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REDACTED – FOR PUBLIC INSPECTION

August 15, 2007

Marlene H. Dortch, Secretary
Federal Communications Commission
445 12th Street SW
Washington DC 20554

Re: *Special Access Rates for Price Cap Local Exchange Carriers*, WC Docket No. 05-25; *AT&T Corp. Petition for Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates for Interstate Special Access Services*, RM-10593

Dear Ms. Dortch:

Attached for filing in the above-referenced dockets, please find an original plus four copies of Qwest Communications International Inc.'s **PUBLIC REDACTED** Reply Comments. Also attached is an additional copy of the Reply Comments to be file-stamped and returned to me.

In accordance with the Commission's July 9, 2007 *Public Notice* in these dockets, I am including another copy of these Reply Comments for delivery to Best Copy and Printing, Inc. Furthermore, the **CONFIDENTIAL UNREDACTED** version of these Reply Comments is being filed under separate cover.

Please do not hesitate to contact me with any questions regarding this matter.

Sincerely yours,

WILKINSON BARKER KNAUER, LLP

Russell P. Hanser

ORIGINAL

REDACTED – FOR PUBLIC INSPECTION

FILED/ACCEPTED
AUG 1 5 2007
Federal Communications Commission
Office of the Secretary

Before the
Federal Communications Commission
Washington, DC 20554

In the Matter of	)	
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To: The Commission

REPLY COMMENTS OF QWEST COMMUNICATIONS INTERNATIONAL INC.

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SUMMARY

No party in this docket has presented any evidence or argument warranting a retreat from the Commission's pricing flexibility regime. Qwest and other incumbent LECs have demonstrated compellingly that their special access rates and per-unit revenues are declining, as one would expect as the efficiencies of a competitive marketplace take hold. The data also demonstrate that the marketplace is competitive, and becoming more so with each passing day. In addition to increasing fiber-optic deployment, the market has seen the advent of competition from cable and wireless providers looking to capitalize on their existing network resources and spectrum holdings to provide high-capacity transmission services.

Given robust competition in the high-capacity transmission market, parties seeking a return to ubiquitous price-cap regulation resort to arguments that have no bearing on this inquiry. These parties attempt to demonstrate, based on ARMIS data, that incumbent LECs' rates of return for special access services are high – but they fail to refute the showings that ARMIS data are completely unsuited for use in this context and, more importantly, that rates of return are in any event irrelevant. They also claim that special access rates must be excessive because they are higher than TELRIC prices for similar services – but they ignore the fact that TELRIC rates were developed for a very different, specific, and statutorily limited purpose. Indeed, re-initializing special access rates at TELRIC levels, as some commenters urge, would be not only unwise but also unlawful.

Critics of the pricing flexibility regime raise other points that, even if they otherwise had merit, simply do not apply to Qwest. Some complain about the terms of incumbent LECs' discount pricing plans, but Qwest's plans do not contain the types of terms at which they direct their ire. The impact of recent mergers in the telecommunications marketplace has also had a unique impact in Qwest's territory. Not having participated in any of the "mega-mergers" of recent years, Qwest now faces significantly *stronger* facilities-based competitors for its special access services. Indeed, Qwest is unique among Bell companies in that it now faces facilities-based, in-region from both Verizon and AT&T, competitors that are significantly larger and better-capitalized that Qwest itself. Thus, the recent merger activity militates in favor of greater regulatory relief for Qwest's special access prices.

Other arguments for increased rate regulation are similarly misguided. Appeals to the Commission's commitment to broadband deployment, for example, turn the Commission's precedent in this area on its head by calling for a more pervasively regulatory environment that will only stifle investment incentives. Calls for greater regulation are particularly ironic coming from the wireless commenters, who consistently advocate deregulation, even for incumbent providers, in proceedings affecting them. There also is no basis for a more granular limitation on the geographic scope of pricing flexibility, as the current MSA test is, if anything, overly conservative, and is in any event complemented by wire-center specific unbundling triggers. There is particularly no reason for a more onerous pricing flexibility standard for special access links serving wireless cell sites, where the incumbent LEC is no more likely than any competing high-capacity transport provider to have facilities already serving the customer's location, and no more able to construct such facilities.

The record demonstrates that Qwest's special access services compete in a highly competitive market for high-capacity transport services. The Commission's pricing flexibility rules should not be rolled back, and indeed should be expanded as described in Qwest's initial comments.

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Washington, DC 20554

In the Matter of	)	
	)	
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To: The Commission

REPLY COMMENTS OF QWEST COMMUNICATIONS INTERNATIONAL INC.

INTRODUCTION

The initial comments in this proceeding confirm that the high-capacity transmission market is competitive and becoming more so, and that incumbent LECs' special access rates are falling. Perhaps in hopes of deflecting the Commission's attention from these uncomfortable facts, parties seeking the re-imposition of ubiquitous rate regulation begin with the conclusory proposition that special access rates are somehow "too high" and proceed to *infer* that the market is not competitive. This approach has no basis in the law, and would lead to bad policy. First, these parties' efforts to "demonstrate" excessive prices are based on irrelevant rate-of-return figures derived from ARMIS data or based on comparisons to TELRIC rates – neither of which were ever meant to be used for this purpose, and both of which suffer from substantial flaws when relied on in this context. Second, even if parties urging a retreat from pricing flexibility could demonstrate a rate of return that could be characterized as "excessive" – which they have not done and cannot do – their evidence would not prove that incumbent LECs exercise market power in pricing flexibility jurisdictions. Simply put, parties seeking to demonstrate market power must demonstrate market power. The facts in this matter preclude any such *demonstration*.

Given the compelling record evidence regarding competition in the high-capacity transmission market (particularly in Qwest's region, where recent mergers have only *strengthened* key competitors) restoration of burdensome price cap regulation in pricing flexibility jurisdictions would be entirely counter-productive. So, too, would restrictions on special access discount plans – in particular those offered by Qwest, which (contrary to mistaken descriptions provided by some in the record) are simple volume and term discounts.

Ultimately, commenters seeking a return to the era of heavy-handed regulation can offer no arguments other than bald self-interest. They would prefer that the rates for their inputs were lower than they are. As a purchaser of special access services outside its region, and of many other inputs in numerous markets, Qwest sympathizes with the desire of all consumers for lower prices. But a desire for lower prices, no matter how strong, does not translate into a public-policy rationale for regulation. In a competitive economy, prices are best set by market forces, not regulators. Especially given the compelling evidence of falling rates and growing competition, the Commission should reject their demands. Instead, it should modify the pricing flexibility regime to reflect the rise of new forms of competition, as described more fully in Qwest's initial comments.

DISCUSSION

I. COMMENTERS HAVE FAILED TO DEMONSTRATE THAT QWEST'S *SPECIAL ACCESS RATES ARE UNREASONABLE.*

A. Commenters Have Not Refuted Evidence that Special Access Rates are Declining.

As Qwest demonstrated in its initial comments, recent data leave no doubt that special access rates are falling.[1] The GAO report cited in the *Public Notice* shows that prices for both DS1 and DS3 channel terminations declined by about 20 percent from the time pricing flexibility was implemented through 2005.[2] Specific data for Qwest's region, based on per-circuit revenues, show similar price drops. For channel terminations plus mileage at the DS1 level, Qwest's average revenue per channel termination across its five largest MSAs (Denver-Boulder, Minneapolis-St. Paul, Phoenix-Mesa, Portland-Vancouver, and Seattle-Bellevue-Tacoma) fell by **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]** percent between 2001 and 2006. The sharpest drops were in Denver-Boulder, where the revenue per termination fell by **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]** percent, and Portland-Vancouver, where revenue fell by **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]** percent. For channel terminations at the DS3 level, Qwest's average revenue per channel termination for the same five MSAs fell by **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]** percent between 2001 and 2006. The biggest drops were in Denver-Boulder, where revenue fell by **[BEGIN CONFIDENTIAL]** [redacted] **[END CONFIDENTIAL]** percent per channel termination, and Seattle-Bellevue-Tacoma, where it fell by **[BEGIN CONFIDENTIAL]** [redacted] **[END**

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[1] *See* Qwest Comments at 4-5, 45-47.

[2] Public Notice, *Parties Asked to Refresh Record in the Special Access Notice of Proposed Rulemaking*, WC Docket No. 05-25, RM-10593 (rel. July 9, 2007), at 2 n.7.

CONFIDENTIAL] percent per channel termination.[3] Importantly, these data are presented in absolute terms, per special access circuit sold, and are not presented on a per-capacity-unit basis. Put differently, the figures above do *not* (as suggested by some commenters[4]) reflect the price of a DS1-equivalent (or DS0-equivalent) provided over an OCn-capacity circuit,[5] but rather the price for a stand-alone DS1 circuit in the relevant market.

In any case, commenters' criticisms of data presented on a per-unit (*i.e.*, "per-DS0 equivalent" or "per-DS1 equivalent") basis are meritless. XO *et al.*, for example, ask why such a "proxy" is needed for special access prices when the "actual data" are available.[6] The data that Qwest has presented regarding its own prices are not proxies, however – they demonstrate actual declines in the price per circuit (again, as represented by revenue) for Qwest's special access services. This is not to say, however, that per-unit prices are irrelevant. The evidence presented in this docket – not least in Qwest's opening comments – demonstrates that capacity needs are increasing as users rely more and more on high-bandwidth video and data applications.[7] In these circumstances, per-unit prices are even more relevant than per-circuit prices, given that the prospects for new deployment at the DS1 capacity level are becoming more and more remote. Under these circumstances, claims that revenues per unit sold are not relevant to an inquiry into the appropriateness of prices for a given commodity are baffling.

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[3] *See* Declaration of Thomas Cogan at ¶ 17 ("Cogan Decl.") (appended to Qwest Comments as Exhibit 1). Other incumbent LECs demonstrate similar declines in their special access prices. *See, e.g.*, AT&T Comments at 22-24; Embarq Comments at 8-11; USTelecom Comments at 13-14; Verizon Comments at 10-14.

[4] *See, e.g.*, Time Warner/One Comments at 34-35.

[5] *See, e.g.*, *id.* at 34-35.

[6] XO *et al.* Comments at 12-13.

[7] *See* Qwest Comments at 39-41.

Parties attempting to obfuscate the fact that special access rates are declining next claim *that incumbent LECs' revenue information is unreliable because the ARMIS data from which it* is derived are either inaccurate or too easy to manipulate.[8] This argument does not apply to Qwest, because Qwest's information on revenues per circuit is based on its customer billing databases, not ARMIS. In any case, this argument is flatly inconsistent with competitors' other claims. In virtually the same breath with which they reject other incumbent LECs' ARMIS-based data, these same critics *dismiss* the incumbent LECs' eerily similar concerns about the use of ARMIS data to demonstrate the rate of return on access services.[9] These parties cannot have it both ways. The reality is that, as Qwest and other incumbent LECs have demonstrated repeatedly in this proceeding, ARMIS data are subject to substantial limitations, deriving both from the parameters of ARMIS reporting itself and from the regulatory structure that determines the ways in which ARMIS data are categorized.[10] Qwest has not relied on such data *either* to assess its revenues *or* to estimate a rate of return.

If anything, the data presented above are likely to understate the degree to which falling special access rates have dropped relative to cost. To the extent that a regulatory regime mandated rates below those that would prevail in a competitive market, rates following deregulation would be likely to rise rather than to fall, reflecting pricing based on market forces rather than external regulatory mandates.[11] Thus, even if commenters *could* demonstrate that

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[8] *See, e.g.*, XO *et al.* Comments at 14.

[9] *Id.* at 12. *See also* Ad Hoc Comments at Appendix 1, A3-A11.

[10] *See, e.g.*, AT&T Comments at 34-36; Embarq Comments at 10-11; Verizon Comments at 41-45.

[11] The Commission has "recognize[d] that the regulatory relief we grant upon a Phase II showing may enable incumbent LECs to increase access rates for some customers," but found that relief "nonetheless is warranted" because, among other reasons, "our rules may have required incumbent LECs to price access

(continued on next page)

special access prices had risen, this would not necessarily demonstrate that these prices exceeded those that would prevail in a competitive market.[12] But as things stand, they have failed to prove even this much: Special access rates are falling, not rising.

B. Incumbent LECs' Rates of Return Are Not Relevant, and in Any Event ARMIS Data Do Not Demonstrate High Rates of Return.

Most crucially, parties advocating increased reliance on price-cap regulation claim that, even if accurate, evidence of falling rates would not be enough to convince them that incumbent LECs lack market power, because they will only be satisfied by an analysis of prices with reference to *cost* or *rate of return*.[13] These claims are also misguided.

First, even if the data presented here demonstrated rates of return that could be characterized as "unreasonable" in other contexts (which they do not), courts have recognized in the antitrust context that proof of high profits alone is never sufficient to establish market power. "Although the consistent extraction of supracompetitive profits may be an indication of anticompetitive market power, such profits could just as easily be obtained as a result of good

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services below cost in certain areas." *In the Matter of Access Charge Reform; Price Cap Performance Review for Local Exchange Carriers; Interexchange Carrier Purchases of Switched Access Services Offered by Competitive Local Exchange Carriers; Petition of U S West Communications, Inc. for Forbearance from Regulation as a Dominant Carrier in the Phoenix, Arizona MSA*, 14 FCC Rcd 14221, 14301 ¶ 155 (1999) ("*Pricing Flexibility Order*"), *aff'd, WorldCom v. FCC*, 238 F.3d 449 (D.C. Cir. 2001).

[12] For this reason, commenters' arguments that rates in Phase II pricing flexibility jurisdictions have risen are of no significance. *See, e.g.*, Sprint Nextel Comments at 16-17; ATX et al. Comments at 7, 10, 49; Ad Hoc Comments at 7. Sprint Nextel, for example, argues that "[i]f the FCC's [pricing flexibility] triggers were reliable indicators of the presence of alternative providers of special access, one would reasonably expect that special access rates in those areas would be lower than the rates charged in areas that did not satisfy the triggers." Sprint Nextel Comments at 16-17. This makes no sense. If rates under pricing flexibility accurately represented rates in a competitive market, one would expect no change following a transition from regulated rates to market rates. And in more likely event that price capped rates were kept artificially low, as predicted by the Commission, *see supra* note 11, one would expect rates to *rise* following regulation, even if the market were indeed perfectly competitive.

[13] *See, e.g.,* Ad Hoc Comments at Appendix 1, A1-A3; XO *et al.* Comments at 14-16.

management, superior efficiency, or differences in accounting, none of which is inconsistent with an efficient market;"[14] thus, "it is always treacherous to try to infer monopoly power from a high rate of return."[15] Indeed, this conclusion should be obvious. "Rate of return" regulation *always* represents a second- (or third- or fourth-) best simulation of competition when competition is absent. It is not meant as an ideal once a market has witnessed the advent of competition. In fact, the foundation of our market economy is the presumption that capital will flow into endeavors promising higher returns than are generally available elsewhere, and that opportunities for revenue will draw in other providers, which will compete against one another and, through competition, transfer value to the consumers. As described in detail in Qwest's initial comments, and as summarized below, this is *exactly* what is happening in the high-capacity transmission markets.

Second, as Qwest observed in its initial comments,[16] a rate-of-return inquiry would be fundamentally misguided in today's telecommunications marketplace. The whole arc of the Commission's special access rate deregulation process, from rate-of-return regulation to price-cap incentive regulation through pricing flexibility, has been designed to move away from the utilities-regulation model used in a prior era and towards a paradigm more similar to that governing other functioning markets showing equally robust competition.[17] Outside the world of

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[14] *Bailey v. Allgas, Inc.*, 284 F.3d 1237, 1252 (11th Cir. 2002) (citation omitted). *See also In re IBM Peripheral EDP Devices Antitrust Litigation*, 481 F. Supp. 965, 981 (N.D. Cal. 1979), *aff'd*, 698 F.2d 1377 (9th Cir. 1983) ("[T]he inference that a defendant that enjoys healthy profits only does so because of an unhealthy market structure is not a strong one. Good management, superior efficiency and differences in accounting provide explanations that are just as plausible, and none of those explanations is inconsistent with an effectively competitive market.").

[15] *Blue Cross & Blue Shield United of Wisc. v. Marshfield Clinic*, 65 F.3d 1406, 1412 (7th Cir. 1995).

[16] Qwest Comments at 4-18.

[17] *Id. See also* AT&T Comments at 41-42.

utilities regulation, in markets showing levels of competition similar to those found in the high-capacity transmission market, firms are never expected to prove up either their costs or rates of return for subcategories of their product offerings. For example, no regulator examines General Motors' costs or rate of return for its light truck line to determine whether the pricing for those trucks is appropriate. Nor do regulators evaluate Coca Cola's rate of return on "Coke Zero," or Kellogg's profits arising from "Frosted Flakes." These companies are unlikely even to maintain data from which a rate of return could be computed.

The rate-of-return inquiry is no more appropriate with respect to the market for high-bandwidth transport services. Qwest and other incumbent LECs have conclusively demonstrated that they face significant competition in this marketplace, and Qwest has shown that it is in fact losing market share to competitors of all stripes.[18] Qwest and the other incumbent LECs also have shown that their revenues for high-capacity circuits are falling across the board. Although special access customers may prefer to pay lower rates for Qwest's high-capacity transmission services, it would be grossly inappropriate for the Commission to impose such rates at this stage, particularly as the market is continuing to exert downward pressure on rates.

C. Reference to TELRIC Rates In the Special Access Context is Misguided, and Reliance on Those Rates Here Would be Unlawful.

Perhaps recognizing the deep flaws in their effort to "calculate" relevant rates of return on the basis of ARMIS "cost" information, various commenters rest their hopes on an even more unlikely gambit: They assert that special access rates should appropriately be compared against TELRIC UNE rates, or – worse – that special access rates should be re-initialized to match those

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[18] *See infra* Part V.

rates. Both of these suggestions are grossly inappropriate, and both conflict with well-settled precedent regarding the section 251 unbundling regime.

1. TELRIC Rates Do Not Provide a Useful Benchmark for Evaluating Special Access Rates.

First, TELRIC rates are an inappropriate yardstick against which to measure special access rates.[19] As the Supreme Court has stated, section 252(d)(1) – the provision that the TELRIC methodology purports to implement – contemplates a form of "ratemaking different from any historical practice," including price caps.[20] Indeed, the Court's ultimate decision that TELRIC represented a reasonable interpretation of section 251(d)(1) was expressly premised on the fact that this provision "is radically unlike all previous statutes," and represented an "explicit disavowal of the familiar public-utility model of rate regulation."[21] Unlike other forms of price regulation meant "to balance interests between sellers and buyers," the point of TELRIC was, in the Court's view, "to reorganize markets."[22] This distinction is perhaps made most explicit in the text of the statute itself: section 251(d)(1) directed the Commission to establish a pricing framework for UNEs "without reference to a rate-of-return or other rate-based proceeding,"[23] and section 251(d)(2) prohibited unbundling of nonproprietary network elements except where competitors would be "impaired" without access.[24]

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[19] *See, e.g.*, Time Warner/One Comments at 30 (expressing alarm that special access rates "are almost universally higher than UNE rates"); XO et al. Comments at 16-17 (reporting that special access channel termination rates "are, with rare exception, significantly higher than … comparable TELRIC-based UNE rates"); ATX et al. Comments at 36-38.

[20] *Verizon Communications Inc. v. FCC*, 535 U.S. 467, 487 (2002).

[21] *Id.* at 489.

[22] *Id.*

[23] 47 U.S.C. § 252(d)(1)(A)(i).

[24] *Id.* § 251(d)(2).

In short, the Supreme Court upheld TELRIC because, and only because, it believed that section 252(d)(1) prescribed a rate-making methodology wholly distinct from those which govern in other contexts. That methodology was intended to apply to incumbent LEC offerings only in the very limited circumstances where a competitor would otherwise be unable to obtain access to such facilities, and where the Commission expressly determined that such pricing was therefore warranted. As such, it should be self-evident that TELRIC UNE rates cannot usefully be compared with rates charged outside the scope of the unique section 251/252 regime.

Comparison to TELRIC rates in the instant context would be particularly worrisome given the likelihood that a move toward TELRIC pricing would greatly undermine the promising deployment described in Qwest's opening comments (and summarized below). As Chairman (then Commissioner) Martin has observed, "the TELRIC pricing formula provides incumbent service providers with an insufficient return on investment capital for new infrastructure," in part because it "fails to accurately measure the true risk of capital investment under current economic conditions."[25] On several occasions, the Commission and the courts have also recognized that TELRIC rates deter investment in new facilities. In its *Notice* seeking comment on proposed modifications to the methodology, for example, the Commission noted that "[t]o the extent that the application of our TELRIC pricing rules distorts our intended pricing signals by understating forward-looking costs, it can thwart one of the central purposes of the Act: the promotion of

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[25] Kevin J. Martin, Comm'r, FCC, Remarks at the 20th Annual PLI/FCBA Telecom Conference (Dec. 12, 2002).

facilities-based competition."[26] And in the *TRRO*, it relied heavily on such disincentives in *eliminating unbundled local circuit switching requirements:*

> [C]ompetitive LECs in many markets have recognized that facilities-based carriers could not compete with TELRIC-based UNE-P, and therefore have made UNE-P their long-term business strategy. Indeed, some proponents of UNE-P effectively concede that it discourages infrastructure investment, at least in some cases. Some competitive LECs have openly admitted that they have no interest in deploying facilities.... The disincentive effects of unbundled local circuit switching are not limited to the deployment of competitive switches, however. For example, even when some competitive LECs acquired a significant number of customers in densely populated areas they never converted to reliance on their own facilities. Thus, unbundled local circuit switching also creates disincentives for competitive LECs to use those competitive switches that have been deployed.[27]

The D.C. Circuit has agreed, repeatedly citing the negative effect that TELRIC pricing has on infrastructure investment.[28] Because TELRIC rates are designed only to serve in the specific and unique ends of sections 251 and 252, they are not a useful reference point from which to assess the reasonableness of special access rates.

2. Re-Initialization at TELRIC Rates Would Flout Judicial and Commission Precedent, Re-Imposing Ubiquitous Unbundling.

Even less plausible than claims that special access rates should be compared to TELRIC UNE rates are claims that special access rates should be re-initialized to *match* those TELRIC

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[26] *Review of the Commission's Rules Regarding the Pricing of Unbundled Network Elements and the Resale of Service by Incumbent Local Exchange Carriers*, 18 FCC Rcd 18945, 18947 ¶ 3 (2003) ("*TELRIC NPRM*"). See also id. at 18949, ¶ 6 (expressing concern that TELRIC rates "might not ... achieve fully the Commission's goal of sending appropriate economic signals.").

[27] *Unbundled Access to Network Elements, Review of the Section 251 Unbundling Obligations of Incumbent Local Exchange Carriers*, 20 FCC Rcd 2533, 2654-55, ¶ 220 (2005) ("*TRRO*"), *aff'd*, *Covad Communications Co. v. FCC*, 450 F.3d 528 (D.C. Cir. 2006), *reh'g denied* (Aug. 17. 2006).

[28] *See, e.g.*, *United States Telecom Association v. FCC*, 290 F.3d 415, 428 (D.C. Cir. 2002) ("*USTA I*"); *United States Telecom Ass'n v. FCC*, 359 F.3d 554, 579 (D.C. Cir. 2004) ("*USTA II*").

rates.[29] This course of action would effectively re-impose universal section 251(c)(3) unbundling obligations for DS1-, DS3-, and OCn-capacity loop and transport facilities – an outcome expressly incompatible with the 1996 Act.

As noted above, TELRIC rates were designed for a specific regulatory purpose. TELRIC rate levels do not permit incumbent LECs to recover their full investments in facilities and undermine competitors' incentives to deploy their own facilities. As a result, use of TELRIC outside of the specific contexts authorized in sections 251 and 252 creates disincentives to investment on the part of incumbents and competitors alike. This is reason enough to reject re-initialization of special access rates at TELRIC levels.

But this course would not only be unwise, it would also be unlawful. Re-initializing special access rates at TELRIC levels would be tantamount to re-imposing ubiquitous unbundling requirements to all high-capacity transmission elements. If incumbent LECs are required to make high-capacity transmission services available at TELRIC rates, it hardly matters whether they are required to do so pursuant to section 251(c)(3) or another statutory provision – the end result is the same. Moreover, all of the well-known costs of section 251(c)(3) unbundling at TELRIC rates would also attend any decision to require TELRIC pricing of special access services. This approach would be blatantly illegal: Section 252(d)(1) specifies that TELRIC pricing is only appropriate where "the failure to provide access to such network

[29] *See, e.g.*, T-Mobile Comments at 14-15; XO et al. Comments at 5; ATX et al. Comments at 39-43. Although it does not expressly call for re-initialization of rates at TELRIC levels, Global Crossing submits that incumbent LECs should be precluded from assessing mileage charges, "since fiber and advanced electronics have largely rendered distance irrelevant to cost." Global Crossing Comments at 8. In effect, this proposal would deny incumbent LECs the opportunity to recoup the fixed costs associated with deploying the facilities used to carry traffic, and force them instead to recoup only incremental costs. In this sense, Global Crossing's proposal shares the flaws of proposals to set special access rates at TELRIC levels.

elements would impair the ability of the telecommunications carrier seeking access to provide the services that it seeks to offer." As the Supreme Court has said, this provision bars any universal application of such rates: "[I]f Congress had wanted to give blanket access to incumbents' networks ..., it would not have included § 251(d)(2) in the statute at all."[30] That section "requires the FCC to apply *some* limiting standard, rationally related to the goals of the Act."[31] Among other things, the courts have instructed the Commission to account for the "availability of elements outside the network"[32] – *i.e.*, of special access offerings.[33] It would be nonsensical, of course, for the courts to have established a "limiting standard" that reversed the statutory test and made unbundled elements available at TELRIC prices in areas where impairment could not be demonstrated.[34]

At the end of the day, commenters' emphasis on low UNE rates merely underscores the fact that proponents of re-regulation are only interested in effecting a wealth transfer, not in sound public policy. In markets where the Commission believes that competitors cannot obtain facilities competitively, they are already entitled to access at TELRIC rates – up until the point at which it becomes efficient to self-provision or obtain elsewhere. To the extent commenters are arguing that they require TELRIC rates universally, they are asking the Commission to impose an unbundling scheme that has already been rejected as unlawful.

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[30] *AT&T Corp. v. Iowa Utils. Bd.*, 525 U.S. 366, 390 (1999)

[31] *Id.* at 388.

[32] *Id.* at 392.

[33] *See, e.g.*, *USTA II*, 359 F.3d at 576.

[34] In fact, this approach would lead inexorably to widespread incumbent LEC bankruptcies, as competitors would enjoy universal access to incumbent LEC facilities at rates assuming the most efficient network available, while the incumbents endured the higher actual costs associated with the facilities being used.

D. The Burden Remains on Parties Urging Repeal of the Pricing Flexibility Rules.

Commenters urging the Commission to re-impose price cap regulation on incumbent LEC special access rates seem to suggest that the burden is on the incumbent LECs to prove that prices justify maintenance of the pricing flexibility regime.[35] In fact, the opposite is true. The Commission adopted the pricing flexibility rules in a notice-and-comment rulemaking proceeding, and those rules were upheld by the D.C. Circuit on appeal. Parties seeking elimination or modification of those rules must present solid evidence of a need for change, but they have failed to do so, and their production of irrelevant arguments has done nothing to shift their burden.

They have argued that special access prices are excessive, but have not rebutted incumbent LECs' evidence that prices are falling. They have argued that prices are above TELRIC, but have not established that TELRIC is remotely relevant. They have argued that incumbent LECs' rates of return for special access services are too high, but they have failed to show that their data are accurate or that rate of return is even relevant. They have argued that incumbent LECs' discount offerings are onerous, but have made no such showing regarding Qwest's offerings.

Parties seeking elimination or modification of the pricing flexibility rules bear the burden of presenting compelling evidence of a need for change. They have utterly failed to do so.

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[35] *See, e.g.*, XO et al. Comments at 2 ("[T]he RBOCs continue to criticize [ARMIS figures] as being 'not right' without providing pricing comparisons or rate of return information they claim *is* right.").

II. DISCOUNT PLANS OF THE SORT OFFERED BY QWEST ARE PRO-COMPETITIVE AND COMMON IN COMPETITIVE MARKETS.

Qwest has responded to competition in the high-capacity transmission market by enacting a variety of customer-focused discount plans. Although certain commenters take issue with incumbent LECs' use of such volume and term pricing plans,[36] the record does not demonstrate that Qwest's special access discounts are in any way discriminatory or problematic. Indeed, very few comments specifically address Qwest's offerings[37] and, where they do, they fail to demonstrate any legitimate concerns.

For example, XO *et al.* criticize Qwest's month-to-month access rates as "so excessive that carriers are induced to commit to a one-year term to gain more reasonable rates."[38] But there are good reasons why the price for a high-capacity circuit, bought on a monthly basis, would be relatively high.[39] The costs of installing such a circuit can be enormous (even more so where, as is sometimes the case with new cell sites in outlying areas, the incumbent LEC has no existing facilities to the customer's location), and can only be recovered in a rational way over a period of months or years. Further, Qwest faces a substantial risk of deriving *no* revenue (or only negligible revenue) from the expensive facility if the customer cancels after only one or two

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[36] *See, e.g.*, ATX *et al.* Comments at 51-52; Time Warner/One Comments at 43-49; XO *et al.* Comments at 28-29.

[37] *See* Sprint Nextel Comments at 7 n.14 (explaining that its criticisms and proposed remedies are focused on carriers other than Qwest).

[38] XO *et al.* Comments at 28. *See also id.* at 29 (criticizing Qwest's Regional Commitment Plan ("RCP") for imposing termination penalties during the first year).

[39] In this way, telecommunications offerings resemble many other offerings. For example, lodging (hotel room vs. rental apartment) and automobiles (rental car versus long-term lease) are substantially more expensive when purchased for only a short term.

months and the facility cannot be reused. Qwest's prices reflect these reasonable economic factors.

It is also critical to bear in mind that Qwest's special access tariffs do not contain some of the terms and conditions that special access customers attack most vociferously. For example, Qwest does *not* offer any pricing plan in either Phase I or Phase II areas that require customers to make a certain percentage of their total telecommunications purchases from Qwest. Qwest only requires commitments in terms of (1) the total dollar value spent or (2) the percentage of DS1 and DS3 circuits taken relative to the customer's purchase level *with Qwest* prior to taking the discount.[40] Contrary to Time Warner's, BT Americas's, and CompTel's implications,[41] Qwest's RCP does *not* require customers to take any specific percentage of their *total* circuit purchases from Qwest. Moreover, UNE circuits are not counted for purposes of the RCP; thus, the RCP does not by its terms inhibit customers from converting or retaining UNE transport circuits. Simply stated, the RCP is an ordinary volume discount plan.

Indeed, criticisms of incumbent LEC discount pricing must be viewed against the appropriate backdrop. Volume and term discounts and packaging arrangements of the sort employed by Qwest are standard elements in virtually every market in all arenas of human endeavor.[42] Every consumer is familiar with them: Cans of soda cost less when purchased by

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[40] This volume commitment is updated periodically thereafter, based on the customer's then-current usage level.

[41] *See* CompTel Comments at 11-12; Time Warner/One Comments at 48; BT Americas Comments at 11. Global Crossing appears to place Qwest in the same bucket as providers employing "total circuit buy" plans, *see* Global Crossing Comments at 9 & n.15, but its description of the RCP itself demonstrates that Qwest's plan is different.

[42] For an extreme example, see *U.S. v. Goodwin*, 317 F.3d 293, 298 (D.C. Cir. 2003) ("a brief review of appellate decisions in narcotics cases suggests that volume discounts are indeed available in the drug world, much as in lawful markets").

the case rather than singly; car insurance is cheaper when the annual premium is paid up front rather than in monthly installments; and French fries and beverages are sharply discounted when purchased with a hamburger. The telecommunications industry is no different – almost a decade ago, the Commission observed that there already was "a substantial body of precedent that promotional programs, volume discounts and other arrangements may be reasonable and non-discriminatory."[43] The Commission has authorized or acknowledged volume and term discounts in a wide variety of contexts, including long distance resale,[44] satellite hardware,[45] satellite services,[46] telephone number pooling administration,[47] CMRS resale,[48] wireline customer premises equipment,[49] and the provision of telecommunications services to schools and libraries that receive universal service support.[50] A similar trend can be observed in the area of the

[43] *Personal Communications Industry Ass'n's Broadband Personal Communications Services Alliance's Petition for Forbearance for Broadband Personal Communications Services, et al.*, WT Docket No. 98-100 *et al.*, Memorandum Opinion and Order and Notice of Proposed Rulemaking, 13 FCC Rcd 16857, 16871 ¶29 (1998).

[44] *See, e.g.*, *Ryder Communications, Inc. v. AT&T Corp.*, 18 FCC Rcd 13603, 13604-05 ¶ 4 (2003); *AT&T Corp. v. Winback & Conserve Program, Inc.*, 16 FCC Rcd 16074, 16075 ¶ 3 n.5 (2001); *American Communication Services, Inc., et al.*, 14 FCC Rcd 21579, 21605 ¶ 53 (1999).

[45] *See, e.g.*, *EchoStar Communications Corporation, et al.*, 17 FCC Rcd 20559, 20635 ¶ 206 (2002).

[46] *See, e.g.*, *IDB Mobile Communications, Inc. v. COMSAT Corporation*, 16 FCC Rcd 11474, 11477-78 ¶ 7 n.28 (2001).

[47] *See, e.g.*, *The Commission Seeks Comments on the Thousands-Block Pooling Administrator Technical Requirements*, 16 FCC Rcd 37101, 3710-11 (2000).

[48] *See, e.g.*, *David S. Poole and Michigan Multimedia & Telecommunications, Inc. v. Michiana Metronet, Inc. and Lucas J. Caruso*, 15 FCC Rcd 9944, 9950 ¶ 16 (1999).

[49] *See, e.g.*, *Interconnection and Resale Obligations Pertaining to Commercial Mobile Radio Services*, 15 FCC Rcd 16221, 16223-24 ¶ 4 (2000).

[50] *See, e.g.*, *Changes to the Board of Directors of the National Exchange Carrier Association, Inc.; Federal-State Joint Board on Universal Service*, 14 FCC Rcd 18756, 18788-89 ¶ 53 n.176 (1999).

package discount plans, which the Commission has approved even in situations where it acknowledged that the market was *not* "fully competitive."[51]

In the specific context of high-capacity transmission circuits, the Commission has permitted volume discounts going back more than twenty years to the early private line rate structure inquiries.[52] Even in those cases, the Commission acknowledged the importance of determining the reasonableness of rates based on a clear-eyed inquiry into rate structure rather than the impact on any particular competitor, noting that there "is a difference between injuring competition and injuring, or even forcing into bankruptcy, a competitor. Inefficient competitors can be driven out of a market by normal price competition; yet, this competition benefits consumers by lowering the price and raising the quality of services and products available to them."[53] The Commission concluded that, while competition is expected to push prices towards forward-looking costs, "'there are legitimate, and in fact compelling, business reasons for pricing products at *or above* their long-run incremental cost.'"[54]

The courts have upheld the Commission's approval of these types of discounts. As Qwest pointed out in its initial comments, the D.C. Circuit recently affirmed a particular BellSouth volume and term discount plan of the type at issue here as reasonable to recover the

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[51] *Bundling of Cellular Premises Equipment and Cellular Service,* CC Docket No. 91-34, Report and Order, 7 FCC Rcd 4028, 4032 ¶¶ 29-30 (1992) (bundling of cellular service with handsets during duopoly era).

[52] *Private Line Rate Structure and Volume Discount Practices,* CC Docket No. 79-246, Report and Order, 97 FCC 2d 923 (1984).

[53] *Id.* at 945 ¶ 36.

[54] *Id.* (emphasis added), *quoting MCI Communications Corp. v. Am. Tel. & Tel. Co.,* 708 F.2d 1081, 1123 (7th Cir. 1983), *cert. denied,* 104 S. Ct. 234 (1983). Indeed, if all products were priced at incremental cost, the economy would collapse, as producers would have no way to recover often-substantial fixed costs.

incumbent LEC's investments in providing special access services, noting that it would be difficult to justify regulation that "frustrat[es] Bell Operating Companies' attempts to maintain stable utilization rates on their networks or to lower their prices" in the special access context.[55] And in 2001, of course, the D.C. Circuit affirmed the Commission's pricing flexibility rules, rejecting essentially the same challenges that are being posed today.[56]

Failing to present a case on common-sense theory or Commission precedent, critics of incumbent LEC discount plans turn to armchair economics. These efforts are similarly unavailing, at least with respect to Qwest's discount plans, which employ volume discounts but in no way endeavor to limit competitors' reliance on third-party facilities or UNEs. Commenters present a "discount foreclosure" theory, suggesting that discount plans preclude them from entering otherwise addressable markets.[57] These commenters contend that volume commitments effectively bundle service in one location (*e.g.*, one route or building) with service to other locations (*e.g.*, other routes or buildings). Such bundling, they assert, are inherently anticompetitive because they foreclose competition in those locations where alternative providers are currently offering service by effectively tying service in these areas to service in other areas where only the incumbent currently operates. This argument, however, ignores voluminous antitrust literature explaining why such discounts are *not* anticompetitive, even if one were to assume (contrary to the facts here) that the discounting provider exercises market power.

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[55] *BellSouth Telecommunications v. FCC,* 469 F.3d 1052, 1056 (D.C. Cir. 2006).

[56] *WorldCom Inc. v. FCC,* 238 F.3d 449 (D.C. Cir. 2001).

[57] *See, e.g.*, Time Warner/One Comments at 43 ("These discounts are structured to ensure that monopoly rates are maintained while keeping CLEC traffic on the ILECs' networks."); Paetec Comments at 13 ("These types of contractual provisions are an ongoing barrier to facilities-based competitive entry because they foreclose competitors' access to customers over the long term and distort entry decisions."); ATX et al. Comments at 9 (claiming BOC efforts to "lock up" customers).

As the antitrust literature makes clear, bundled discounts serve many legitimate business purposes. As Professors Areeda and Hovenkamp explain in what CompTel terms "[t]he leading treatise on antitrust law,"[58] "[b]undling serves a number of procompetitive or competitively benign purposes, including achievement of scale or scope economies...."[59] For this reason, "most tying arrangements are legal."[60] As another commentator writes, "Package discounting is a common phenomenon among firms that have no predatory ambition. It is a business strategy that often makes perfectly good economic sense without any need for injury to a rival."[61] Of course, the chief benefit of discounts – here as in any other market – is to increase consumption of one's offering. "[T]he bundled discount enables the firm to sell more, and in the presence of economies of scale it can then [supply the offering] at a lower price. A purchaser who receives a large discount across the board for purchasing an aggregation of products A and B will very likely purchase more of each."[62] Thus, "[u]nlike ... below-cost [*i.e.*, predatory] pricing, which is

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[58] CompTel Comments at 13-14.

[59] PHILLIP E. AREEDA AND HERBERT HOVENKAMP, ANTITRUST LAW: AN ANALYSIS OF ANTITRUST PRINCIPLES AND THEIR APPLICATION ¶ 749 at 261-62 (Aspen Supp 2004) ("AREEDA & HOVENKAMP"). *See also* Daniel A. Crane, *Multiproduct Discounting: A Myth of Nonprice Predation*, 72 U. Chi. L. Rev. 27, 43 (2005) ("Firms regularly employ mixed bundling strategies for all sorts of reasons that antitrusters would rate from neutral to procompetitive.") ("*Multiproduct Discounting*"). Notably, CompTel focuses exclusively on AREEDA & HOVENKAMP's view on when a tying arrangement may be said to exist, ignoring entirely the more critical discussion that follows, which addresses when such a tying arrangement may be deemed anticompetitive. CompTel Comments at 13-14. As Areeda and Hovenkamp remind us, "[e]ven when a 'tie' is found, whether by contract, discount, or technological design, *most tying arrangements are legal.*" AREEDA & HOVENKAMP ¶ 749 at 261 (emphasis added).

[60] AREEDA & HOVENKAMP ¶ 749 at 261.

[61] *Multiproduct Discounting* at 48.

[62] AREEDA & HOVENKAMP ¶ 749 at 262. *See also Multiproduct Discounting* at 40 ("Diversified firms may achieve economies of scope or scale, reduce transaction costs, or stimulate demand by selling products in a package.").